TRANSCRIPT OF RECORD

Supreme Court of the United States

OCTOBER TERM, 1960

No. 533

UNITED STATES, PETITIONER,

vs.

STANLEY S. NEUSTADT, ET AL.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

PETITION FOR CERTIORARI FILED NOVEMBER 17, 1960
CERTIORARI GRANTED DECEMBER 19, 1960

Supreme Court of the United States

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INDEX

[fol. 1] (File Endorsement Omitted)

IN THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF VIRGINIA

Civil Action No. 1719

STANLEY S. NEUSTADT,
ROSE-BARBARA Y. NEUSTADT, PLAINTIFFS

v.

THE UNITED STATES, DEFENDANTS

COMPLAINT—Filed June 17, 1958

Come now the plaintiffs, by their attorney, and for their complaint against the defendant respectfully aver:

1. The plaintiffs are citizens and residents of the State of Virginia.

2. This case arises under the Federal Tort Claims Act, as amended (28 U.S.C. § 1346(b) and 28 U.S.C. Chapter 171).

3. On or about April 9, 1957 the plaintiffs entered into a contract for the purchase of a house and lot from Colonel and Mrs. Elmer Almquist, located at 1408 Oakcrest Drive, Alexandria, Virginia. The contract provided that the sale was conditioned upon the plaintiffs' obtaining a loan secured by a mortgage on the property with a term of thirty years, in the amount of eighteen thousand eight hundred dollars ($18,800.00), which loan and mortgage was to be insured by the Federal Housing Administration pursuant to the provisions of Title II Section 203 of [fol. 2] the National Housing Act, as amended (12 U.S.C. § 1709) and to conform with all of the provisions of that Act and the regulations issued thereunder.

4. The contract also provided that the seller would deliver to the plaintiff, prior to the sale of the property, a written statement setting forth the amount of the appraised value of the property as determined by the Federal Housing Commissioner.

5. At the time the contract was entered into, plaintiffs were advised and understood that before the Federal Housing Administration would enter into a contract of insurance with respect to a mortgage on a particular single-family dwelling, an employee of the Administration would make a careful physical inspection of the premises for the purpose of appraising the property and fixing its fair market value. Plaintiffs were also advised and understood that in the event the said inspection revealed any structural deficiency, substantial defect or other condition that would materially affect the fair market value of the property, the useful life of the property, or the eligibility of the property as security for a loan to be insured by the Federal Housing Administration, the defect or condition would be noted upon the appraisal or underwriting report made by the inspector and, if the condition could be satisfactorily corrected, the agreement to insure the loan by the Federal Housing Administration would be conditioned upon the correction of the defect or condition.

6. Plaintiffs relied upon the provision of the contract of sale that a statement of the amount of the appraised value of the property would be furnished to them and upon the fact that any substantial deficiency or defect in the property would be disclosed as the result of the inspection and appraisal made by the defendant in that they were not obligated to purchase the property if any such deficiency or defect existed and remained uncorrected.

[fol. 3] 7. Some time prior to March 14, 1957, an inspection of the property was made by the Federal Housing Administration and an appraisal and underwriting report was made in consequence of which the property was found to be eligible for mortgage insurance. The property was appraised at $22,750, and the condition of the property was certified in said report to be good. No condition requiring the correction of any deficiency or other similar defect was imposed by the Federal Housing Administration upon its execution of a contract of insurance upon the loan and mortgage covering the property.

8. Plaintiffs thereupon purchased the said property on July 2, 1957 for the total price of $24,000.00 of which $18,800.00 was borrowed upon the security of a mortgage insured by the Federal Housing Administration. Plaintiffs took possession of the property on that date and have resided therein since July 10, 1957.

9. At the time of the inspection of the property by the Federal Housing Administration, there did, in fact, exist a substantial and serious structural defect which should have been apparent to any person reasonably familiar with the construction and appraisal of single-family dwellings and particularly to a person whose occupation involved the inspection and appraisal of houses of this general character. The defendant, through its representatives, conducted its inspection of the property in so negligent and careless a fashion as to fail to observe that the foundation of the building had failed some time in the past and that there was reason to believe that another such foundation failure might occur in the reasonably near future. An inspection conducted with ordinary care would have disclosed this condition and would have resulted in the refusal of the Federal Housing Administration to insure the mortgage.

[fol. 4] 10. As the result of the negligence of the defendant, the plaintiffs have been damaged in that the fair market value of the property on or about July 2, 1957 was not more than $13,000.00 and plaintiffs would not have been obligated to purchase and would not have purchased the property for $24,000 but for the carelessness and negligence of the defendant.

WHEREFORE, plaintiffs demand judgment against the defendant in the amount of $11,000.00 and for such other and further relief as to this Court may seem proper.

/s/ Lawrence J. Latto
LAWRENCE J. LATTO
928 South 26th Street
Arlington, Virginia
Attorney for plaintiffs

[fols. 5-19] • • • •

[fol. 20] (File Endorsement Omitted)

IN THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF VIRGINIA
Alexandria Division

(Title Omitted)

ANSWER—Filed Jan. 2, 1959

Now comes the United States by its attorney and answers the complaint herein as follows:

FIRST DEFENSE

The complaint herein fails to state a claim upon which relief can be granted.

SECOND DEFENSE

Any damage sustained by the plaintiff herein as described in the complaint was caused in whole or in part, or was contributed to, by the negligence or fault or want of care of the plaintiff and not by any negligence or fault or want of care on the part of the defendant.

THIRD DEFENSE

The complaint herein seeks to impose liability on the United States in a cause of action to which the United States has not waived its sovereign immunity.

FOURTH DEFENSE

The acts complained of as being negligent were in fact the result of use of reasonable care on the part of agents and employees of the United States and were not negligent acts.

Defendant has no knowledge or information sufficient to form a belief as to the nature or extent of the plaintiff's damage, if any and therefore denies the allegation of damage in the complaint.

FIFTH DEFENSE

1. Admits paragraph one of the complaint.

2. Denies that statutes referred to in paragraph two give jurisdiction to this Court to grant relief in this cause.

[fol. 21] 3. Admits paragraph three of the complaint.

4. Admits paragraph four of the complaint.

5. Defendant has no knowledge or information sufficient to form a belief as to the allegations of paragraph five, therefore, denies each and every allegation of paragraph five.

6. Defendant has no knowledge or information sufficient to form a belief as to the allegations of paragraph six, therefore, denies each and every allegation of paragraph six.

7. Admits paragraph seven of the complaint.

8. Admits paragraph eight of the complaint.

9. Defendant has no knowledge or information sufficient to form a belief as to the allegations of paragraph nine, therefore, denies each and every allegation of paragraph nine.

10. Denies paragraph ten of the complaint.

WHEREFORE, having fully answered, the defendant prays that the cause be dismissed with costs to the plaintiff.

/s/ Henry St. J. FitzGerald
HENRY ST. J. FITZGERALD
Assistant United States Attorney

CERTIFICATION OF SERVICE OMITTED IN PRINTING

[fols. 22-23] • • • •

[fol. 24] (File Endorsement Omitted)

IN THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF VIRGINIA
Alexandria Division

(Title Omitted)

MOTION OF THE UNITED STATES FOR LEAVE OF COURT TO AMEND ANSWER—Filed March 20, 1959

The United States of America, defendant herein, by its attorney, Henry St. J. FitzGerald, Jr., Assistant United States Attorney in and for the Eastern District of Virginia, moves the court for leave to amend its answer on file herein in the following particular:

Adding two defenses to the complaint herein in the language as follows:

SIXTH DEFENSE

The complaint herein seeks to impose liability on the United States in a cause of action to which the United States has not waived its sovereign immunity in that the acts or omissions alleged in the complaint are such as would fall within the exclusionary provisions of Section 2680, Title 28, United States Code, and particularly subsection (a) thereof.

SEVENTH DEFENSE

The complaint herein seeks to impose liability on the United States in a cause of action to which the United States has not waived its sovereign immunity in that the provisions of Section 2680, Title 28, United States Code, and particularly, the provisions of Subsection (h) thereof, exclude from the coverage of the Federal Tort Claims Act, any claim against the United States arising out of misrepresentation or deceit.

/s/ Henry St. J. FitzGerald
HENRY ST. J. FITZGERALD
Assistant United States Attorney

[fol. 25]

POINTS AND AUTHORITIES IN SUPPORT OF MOTION TO AMEND ANSWER

For points and authorities in support of this motion the United States relies upon Rule 15 (a) of the Federal Rules of Civil Procedure.

/s/ Henry St. J. FitzGerald
HENRY ST. J. FITZGERALD
Assistant United States Attorney

[fol. 26] (File Endorsement Omitted)

IN THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF VIRGINIA
Alexandria Division

(Title Omitted)

ORDER GRANTING LEAVE TO AMEND—Filed March 26, 1959

This cause came on to be heard on the defendant's motion for leave to amend its answer on file herein, and it appearing that justice requires that such an order be given and the court being fully advised, it is hereby

ORDERED that the defendant's answer be and hereby is amended by adding the following two defenses as if they were included in the answer as filed:

SIXTH DEFENSE

The complaint herein seeks to impose liability on the United States in a cause of action to which the United States has not waived its sovereign immunity in that the acts or omissions alleged in the complaint are such as would fall within the exclusionary provisions of Section 2680, Title 28, United States Code, and particularly subsection (a) thereof.

SEVENTH DEFENSE

The complaint herein seeks to impose liability on the United States in a cause of action to which the United States has not waived its sovereign immunity in that the provisions of Section 2680, Title 28, United States Code, and particularly, the provisions of Subsection (h) thereof, exclude from the coverage of the Federal Tort Claims Act, any claim against the United States arising out of misrepresentation or deceit.

/s/ Albert V. Bryan
United States District Judge

Charleston, S. C.
March 26, 1959

Plaintiffs, by their counsel, consent to the entry of this order.

/s/ Lawrence J. Latto

[fo]s. 27-50]

[fol. 51] (File Endorsement Omitted)

IN THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF VIRGINIA
At Alexandria

Civil 1719

STANLEY S. NEUSTADT and
ROSE-BARBARA NEUSTADT

v.

UNITED STATES OF AMERICA

MEMORANDUM BY THE COURT—Filed Oct. 20, 1959

The plaintiff-purchasers qualified for, and were entitled to, "a written statement setting forth the amount of the appraised value of the property as determined by the Commissioner" of the Federal Housing Administration. This was a right conferred upon them not by their contract alone but also by section 226 of the National Housing Act. 12 USCA 1715q, as added August 2, 1954. This statutory provision was intended to give a purchaser the benefit of the Government's appraisal as a guage of the fairness of the price he is paying. See Senate Report and Conference Report on 1954 amendment, pp. 2726 and 2828, respectively, of 2 United States Code Congressional and Administrative News, 83d Congress, 2d. Ses. 1954. Of course the statute meant an appraisal made with ordinary care and diligence. A fair appraisal here certainly necessitated an inspection of the property. For negligence by the Commissioner in the performance of this duty the United States is liable to the purchasers.

Such an appraisal is not merely a representation—any more than the marking of a wreck or the absence of a navigational aid is a representation to a mariner of the [fol. 52] presence or non-existence of a peril. Cf. Indian Towing Co. v. U.S., 350 U.S. 61 (1955) and Somerset Seafood Co. v. U.S., 193 F.2d 631 (4 Cir. 1951). A careful inspection of the property was a positive act required of the Commissioner by section 226 as a direct and im-

mediate service to the plaintiff-purchasers. His responsibilities to them were those due by a professional appraiser privately employed by a vendee; the Government's liability is the tort liability of the privately employed appraiser for negligence. 28 USCA 2674. The Commissioner's carelessness cannot be classed as a misrepresentation merely because the result is embodied in a report. Hence, there is no escape for the United States through the Federal Tort Claims Act's exception of liability for misrepresentation. 28 USCA 2674, 2680(h).

Paradoxically, the liability of the Government for a tort of the kind here is underscored by the terms in which section 2680(a) of the Act excepts from its acceptance of responsibility any claim, such as the plaintiffs', arising from an omission of a Government employee while executing a statute. The exemption is accorded only so long as the employee was "exercising due care". The finding of negligence here thus proves both the suability and the liability of the Government.

The evidence clearly estabilshes that the plaintiffs in good faith relied upon the Commissioner's appraisal in consummating their contract of purchase. Rightfully they assumed that the Cominissioner's appraisal followed a diligent and painstaking examination of the property. That there were serious structural defects in the house has been preponderantly proved. The evidence likewise shows that reasonable care by a qualified appraiser [fol. 53] would have warned them of the defects. From the evidence the court fixes the fair market value of the property, as of the time of the settlement of the contract, at $16,000.00. As the plaintiffs paid $24,000.00 in the acquisition of the property, they have suffered as a direct result of the negligent appraisal a loss of $8,000.00.

No discussion is needed of the defense of contributory negligence. It was not stressed at the trial, and the structural weaknesses in the building were not readily visible to a vendee inexperienced in construction. Nor, obviously, is the Government's argument sound for exemption under the "discretionary function or duty" provision of section 2680(a), Federal Tort Claims Act. Again, the court deems it unnecessary to discuss the additional

ground of liability pleaded by the plaintiffs: that the Federal Housing Administration having customarily undertaken to advise purchasers upon the condition of properties appraised by the Commissioner, and having so assumed this responsibility, even though as a volunteer, the United States is liable for any negligence of the Administration in this practice.

Adopting this memorandum as a statement of its findings of fact and conclusions of law, the court will enter a judgment for the plaintiffs against the United States in the sum of $8,000.00, with such interest and costs as are allowed by statute. Plaintiffs' attorney will present an appropirate order within fifteen (15) days, first submitting it to opposing counsel for comment as to form.

/s/ Albert V. Bryan
United States District Judge

October 20th, 1959.

[fol. 54] • • • • •

[fol. 55] (File Endorsement Omitted)

IN THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF VIRGINIA
At Alexandria

Civil 1719

STANLEY S. NEUSTADT and
ROSE-BARBARA NEUSTADT

v.

UNITED STATES OF AMERICA

FINAL ORDER ON TRIAL AND JUDGMENT—Nov. 30, 1959

This action having come on for trial before the Court, without a jury, the Honorable Albert V. Bryan presiding on June 24 and 29, 1959, the parties having appeared by their respective counsel, and having proceeded with the introduction of evidence, and the Court having heard all of the evidence and the arguments of counsel;

And the Court having on October 20, 1959 filed its memorandum opinion, and the Court having adopted said memorandum as a statement of its Findings of Fact and Conclusions of Law and found that the plaintiffs are entitled to a judgment against the United States in the sum of $8,000.00, with such interest and costs as are allowed by statute;

And the plaintiffs having filed their bill of costs in the total amount of $28.00 and the Clerk of this Court having duly taxed and allowed the same, it is hereby

ORDERED, ADJUDGED and DECREED this 30th day of November, 1959, that Stanley S. Neustadt and Rose-Barbara Y. Neustadt do recover of and from the United States of America the sum of $8,028.00, with such interest thereon as is authorized by law.

/s/ Albert V. Bryan
United States District Judge

Alexandria, Virginia.
November 30, 1959.
Approved as to form:

/s/ Henry St. J. FitzGerald
United States Attorney

[fols. 56-61] * * * *

[fol. 1] (File Endorsement Omitted)

IN THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF VIRGINIA
ALEXANDRIA DIVISION

Civil Action No. 1719

STANLEY S. NEUSTADT and
ROSE B. Y. NEUSTADT, PLAINTIFFS

vs.

THE UNITED STATES OF AMERICA

REPORTER'S TRANSCRIPT

Before
United States District Judge
Hon. Albert V. Bryan
June 24 and 29, 1959

APPEARANCES:

LAWRENCE J. LATTO, ESQ.,
For the plaintiffs.

HENRY ST. J. FITZGERALD, ESQ.,
Assistant United States Attorney,
For the United States of America.

[fols. 2-5] * * * *

* * * *

[fol. 6] STANLEY S. NEUSTADT

was called as a witness by counsel in his own behalf and, having been first duly sworn, was examined and testified as follows:

DIRECT EXAMINATION

BY MR. LATTO:

Q. Would you state your full name, please?
A. Stanley S. Neustadt.

Q. And where do you reside, Mr. Neustadt?
A. 1408 Oakcrest Drive, Alexandria, Virginia.
Q. What is your profession?
A. I am an attorney.

• • • •

Q. Mr. Neustadt, you are the owner of the premises at 1408 Oakcrest Drive in Alexandria?
A. That is right, I am.
[fol. 7] Q. When did the purchase of this house first come under your consideration?
A. It was during the middle part of March in 1947 that we first were aware that this house was for sale and considered purchasing it.
Q. And can you describe briefly the negotiations leading up to the making of an offer on your part and on the part of your wife for the purchase of this house?
A. Well, my wife and I had been trying to find a home to purchase for some time, and had left our names with several real estate agents, and on the 14th of March one of these agents, a Mrs. Rena Hubbard of Hubbard Realty Company called my wife to suggest that there was a house in the area in which we were interested and which was for sale, which my wife might be interested in. My wife accompanied Mrs. Hubbard to this house which was just a few streets from where we then lived in an apartment.
During the afternoon and immediately upon her return home, called me at the office, and told me about the house, and we arranged that that evening after I returned from work I would go to look at the house with Mrs. Hubbard, which I did.
At the time I went to see the house it was, as I say, in the evening, and we met the current owners, Colonel Ormquist, who at that time was the owner of the house, showed me through the house. I looked at all the bed-[fol. 8] rooms and the other rooms in the house, and looked cursorily at the basement. I couldn't see much about the outside of the house because, as I say, it was 8:30 or 9:00 o'clock in the evening, and I returned home and agreed with my wife's impression that this house seemed to meet all of our requirements.

We discussed the matter with Mrs. Hubbard. There was, of course, a question of the financial arrangements and although the price at which the house was offered was substantially in excess of what we had considered, we were able to afford, it was suggested to us that if we made a slightly lower offer and were able to get a 30-years mortgage insured by the F.H.A., that the down payment, both the down payment which we would have to make and the monthly payments under the mortgage or deed of trust would be within our means.

Q. Had you discussed the terms of financing with the then owners of the house at the time of your visit?

A. No, indeed. At no time did we ever discuss the financing terms with the owners. As a matter of fact, that evening was the only time I saw the Ormquists until we had an effective contract after the final arrangements for the purchase had been made. We saw them once again. But at that time everything was set except for the actual settlement.

As I say, we considered that evening the desirability of the house and our ability to purchase it, and I might point out that both—well, I at least had been raised in [fol. 9] an apartment and knew very little about homes. I considered the possibility of hiring someone to inspect the house in order to ascertain whether it was structurally and otherwise sound, but it was my understanding that one of the Virginia F.H.A. financing, such as we contemplated, was that the F.H.A. appraisal which was necessary, would disclose matters of the kind about which I had any concern at all, so that it would not be necessary for me to hire an expert.

Q. Had you—

A. Along this line.

Q. Had you been advised that an F.H.A. appraisal of the house had been made?

A. Yes, indeed. The reason that we even considered making an offer for the house in view of the price at which it was being offered was our understanding that an F.H.A. appraiser had been there quite recently and that the then owners of the house were, had started the process of acquiring the necessary F.H.A. preliminary steps

so that the house could be sold with an F.H.A.-insured mortgage.

Q. Did you then make an offer for the house?

A. The following day after my wife and I considered this further, since it was an important step to us, we did, through the Hubbards, make an offer for the house. Our offer was expressly conditioned upon the obtaining of the kind of financing to which I referred, namely, an F.H.A. [fol. 10] appraisal in the amount of our offer with the largest first trust which F.H.A. would permit under such an appraisal and consequently, the smallest down payment.

Q. Was the price which you offered at this time the price which you ultimately paid for the house?

A. No, indeed. The price we offered at that time was $24,500, and the reason that we—well, I might say that our offer was accepted within a very short time, within just a few days. The Ormquists accepted our offer and the only thing that remained at that time was for the F.H.A. appraisal to be finished so that we'd know whether the conditions of the contract were fulfilled. It turned out that they were not because the F.H.A. appraisal which should have been $24,500 for the terms of our condition to become effective was not $24,500 but rather $22,750. With this appraisal the financing which we contemplated was impossible. So that at that point we stood about where we were when we started. It was agreed by everybody that no contract existed.

• • • •

[fol. 11] THE COURT: Let it be admitted.

(The Clerk so marked the document as Plaintiffs' Exhibit No. 1.)

BY MR. LATTO:

Q. Following the receipt of the information of the F.H.A. appraisal would not permit the purchase of the house under the terms of the financing provided in this contract, did you have further negotiations with the Ormquists, either directly or through the brokers?

A. Yes, we did. The F.H.A. appraisal which had now been made known resulted in a certain maximum first

trust which they would insure on the basis of—we now knew what the largest first trust we could acquire would be—on this basis, and with knowledge of our cash position we decided to make another lower offer for the home since we were not in a position to make any greater down payment than we had originally decided upon.

Q. Let me ask you this first. Did the fact that the F.H.A. appraisal was less than you had anticipated give you any concern?

A. It gave me very grave concern. It, as I indicated, we were novices in this area, and before we decided to make a second offer for the home, it occurred to me that the difference between the price which we had originally offered and which we thought the F.H.A. would appraise the house at and the amount which the F.H.A. finally appraised the house at may have been due to the exist- [fol. 12] ence of some flaw in the house which was deemed to reduce its value to that extent because we were concerned lest we would buy a house with some flaw which needed immediate or even ultimate repair. I established to my satisfaction that the lower appraisal did not in fact and could not in fact represent the difference in an appraisal, could not represent the existence of such a defect.

Q. Just how did you establish this to your satisfaction?

A. Well, the first thing I did was call the agents and ask them. However, in addition to that I called the vice president of one of the vice presidents of the bank where I maintained an account which has a large real estate department, and ask him point-blank whether the lower appraisal might reflect such a thing. And I also called one of the larger mortgage companies in Washington and asked the same question. In all instances I was assured that the practice of the F.H.A. in the event a defect in the house was—

• • • •

THE WITNESS: I was assured that if there were a defect it would not—defect, some substantial structural— [fol. 13] or other defect in the house it would not be reflected in a lower appraisal but rather a condition on the F.H.A.'s commitment to insure that the appraisal

would reflect the value of the house in sound condition and that if it were not sound, the commitment to insure would be conditioned on correction of the defect. The appraisal would not be affected by this. Once my wife and I became convinced of this; with the knowledge we then had, and we asked specifically, I might add, whether there was such a condition in this case and was informed it was not—once we were convinced that the appraisal did not indicate any unsoundness in the home, we did, as I say, make another offer at a lower total price.

BY MR. LATTO:

Q. Was that offer accepted?

A. This offer was not accepted. This offer was rejected, I understand, by the Ormquists.

Q. Well, let's see if we can speed this up.

Did you ultimately make an offer which was accepted?

A. After that offer was rejected, we made still a third offer which was accepted.

• • • •

[fol. 14] • • • •

• • • •

[fol. 15] BY MR. LATTO:

Q. Did you take possession of the house in accordance with the contract just admitted in evidence?

A. We did.

Q. About what time was that?

A. Well, we settled on July 2nd, 1957, but we didn't actually move our family into the house until the 10th of July of the same year.

• • • •

[fol. 16] Q. What was the general condition of the house at about the time you took title or moved into it, so far as the need for decorating, so on, general appearance as it appeared to you?

A. Well, on the 2nd of July after we took title, later in the day, my wife and I had the keys and we went over to look at the house expressly in order to see whether possibly any redecoration was necessary and we inspected

the house quite carefully, and we found absolutely nothing which would indicate the necessity for any redecoration at all. The walls, the interior walls of the house had all been relatively recently painted. We'd been told that they had been painted just before we first saw the house in March. House was immaculately clean and the walls and the ceilings, as I say, looked fine to us.

I did notice on that day for the first time a crack on the inside wall of the basement on the east side of the house, but it was a crack which had been filled in or pointed up, and as I say, the house seemed to be in very nice condition.

Between the 2nd of July and the 10th when we actually [fol. 17] moved in I took over some of our more fragile belongings which we didn't want the movers to take over and stored them in the what we call the sun parlor. It's an enclosed porch just off the living room, and when I stored these things in the sun parlor I noticed that the floor of the sun parlor sloped toward the front of the house a little bit, but other than these things that I have mentioned we did not notice anything untoward about the house. Until we moved in on the 10th with all of our belongings.

Q. How soon after you moved in on the 10th did you begin having problems with the house?

A. We, we remember very vividly the second night that we were there, which I think would be the evening of the 11th of July. A crack appeared in the plaster over the door which connects the living room with this sun parlor that I referred to. It was fairly deep crack which extended from the ceiling to the top of this door which I mentioned. Wtihin a day or two thereafter another crack opened on the opposite wall of the living room near the back of the house, which during the course of a day or two spread from the ceiling to the floor of the living room and not in a straight line. It would have been kind of a jagged line. My wife and I were upset about these cracks, but our initial thought was that they may have resulted from improper patching of the plaster when the house had last been redecorated. These cracks got wider [fol. 18] within the succeeding few days and at one point some of the plaster dropped to the floor from the crack

on the wall of the living room, and we starting getting cracks in the ceiling. And my wife became very concerned lest our children who are very young might be hit by some of this plaster, so we proceeded to try to see what we could do about fixing it.

Q. Did you call someone about making repairs to the plaster?

A. That is exactly what we did. We got the name of a plastering contractor and asked him to come look at the problem we had and took him a little while before he showed up, and in the meantime we contacted a second plastering contractor and then the first one showed up and he examined these cracks and he said to us that he would not undertake to repair them without some assurance from an architect or a builder that they would not immediately reopen because in his judgment they were certainly not due to any improper patching of the plaster. They were due to some basic defect in the house and that it would be a complete waste of time and money to try to just, to go ahead and try to patch the plaster without finding the basic cause of the cracks.

When the second plasterer showed up he gave us essentially the same information. So we started to try to find out what could be done. While all this was going on every day a new crack in the plaster appeared, and [fol. 19] finally we noticed that the basement walls, the inside which are cinder block which had been painted with a yellowish or tannish coat of Sta-Dri paint had also cracked fairly severely, and we became very worried about this. And the first person we contacted was the builder of the home of one of our neighbors.

She happened to know this gentleman and suggested that we should call him, which I did. He came out and looked at the house and he told us that there was something very basically wrong with the house. He wasn't completely certain what it was, but his advice to us was to fix the house up so it looked half-way decent and sell it immediately.

Of course, this was advice which we could hardly follow. We—sounded fraudulent in the first place, and second place, we had just moved into the house and we wanted

to live there if we could, and seemed like a snap judgment on his part, so I consulted another builder, who looked at the house more carefully and informed us that in his judgment the problem might result either from the roots of a large oak tree which stands in front of our house, or he thought more probably from some condition which had to do with the water content under our, and around the house. However, he wasn't in a position to really make a careful analysis of the problem and advise us on it, but he did feel that it was serious enough for us to exert every effort, whatever necessary expense.

Q. Did you consult at any time or about this time with [fol. 20] officials of the Federal Housing Administration?

A. Immediately thereafter I called the mortgage broker which at that time held our mortgage or our trust, and he suggested that I contact a Mr. Elliott at the F.H.A. who at that time I believe was the chief underwriter in the Washington Office of the F.H.A.

I called Mr. Elliott, explained what had occurred, and the advice that I had received, and he assured me that he would send out to our house an F.H.A. inspector who would look the place over and see what, if anything, needed to be done or could be done.

A few days later an inspector from the F.H.A. did come out to look at the house. His name was Harrison Jacobs. Mr. Elliott had assured me that Mr. Jacobs was the best inspector the F.H.A. had in this area, and by the time Mr. Jacobs arrived, I might add, there wasn't a room or a ceiling in the house that didn't have substantial cracks in the plaster. The basement walls all had cracks in the ciner block. The condition of the house had deteriorated to a frightening extent.

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[fols. 21-23] * * * *

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[fol. 24] Q. Bring you back now to the first visit by Mr. Jacobs. About how long did he spend at this time?

A. Well, my recollection isn't precise on this, but I am sure he was at the house for at least an hour, and possibly somewhat longer.

He inspected the house, it seemed to me, very carefully, measured it, how much the front wall and the basement had been pushed in, examined the floor of the basement very carefully and indeed the remainder of the house, all of the plaster cracks.

Q. Did he give you any advice at this point?

A. Yes, he did. He told me that it was obvious that a serious blunder had been made, * * *

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[fol. 25] Q. And were subsequent visits to your house by officials or employees of the F.H.A.?

A. Yes, there were. After I had written the letter, Mr. Jacobs returned on one occasion with a Mr. Simpson who I was told was the F.H.A.'s chief architect, and Mr. Henjun, who was not connected with the F.H.A. but who was the original builder of the home.

We had found out that the home was built in 1941 and that Mr. Henjun was the builder.

On this occasion the three gentlemen dug down on the outside of the house. Well, they didn't do it. They had a laborer that did it, dug down by the oak tree to ascertain whether it might be the roots of the tree and which were causing the trouble, and they decided that it was not. They also had a small hole broken through the concrete in the basement floor and examined the nature of the soil underneath the basement floor, and as a result of this visit which lasted well in excess of an hour also, they prepared a report which was later shown to me about what they thought the cause of the trouble was and how it might be possible, be remedied.

[fol. 26] Q. Did you receive a copy of that report?

A. Yes, I did.

* * * *

Q. Yes, do you want to say something else?

[fol. 27] A. Yes, I would like to add, I think I got the chronological—a little bit wrong—nothing that I have said so far is inaccurate, but between the time that Mr. Jacobs first came to the house and the time that Mr. Simpson and Mr. Henjun came with Mr. Jacobs, I believe that between that time there was a conference at my home between Mr. Jacobs, Mr. Elliott and Mr. Elliott's assistant,

a Mr. Slate. They all came out to my house at that time. Mr. Elliott and Mr. Slate saw the house for the first time. Mr. Slate, I recall, took some pictures, the various cracks in the basement?

Q. Was that during the day or during the evening?

A. This was during the day. I came home from the office again and during the course of this discussion it was again stated to me that a serious mistake had been made, that these gentlemen wished to do whatever they could to help me in my trouble. It never was made at all clear to me what they could do but it was subsequent to this time that they persuaded Mr. Henjun to come out and look at the house.

Q. Let me ask you this. You testified earlier that you were aware of the fact that if a house had a substantial defect, it would probably be revealed by the inspection made by the F.H.A., didn't you raise this question with Mr. Jacobs or Mr. Elliott or Mr. Slate or any of the other officials that you spoke with?

A. I am quite sure that I mentioned the fact that this [fol. 28] must have been the kind of thing that should have been ascertained at the inspection, and none of them ever suggested that I was wrong about this. Quite the contrary. They led me to believe that in fact a failure to discover this was the mistake or the blunder which they were talking about.

I might point out that among the first things that Mr. Jacobs noticed about the house when he saw the basement were these I-beams which I have referred to which are shown in Exhibits 9 and 10, which he informed me were obviously constructed after the house was originally constructed. They were not part of the original structure of the house, in other words. He also pointed out to me that the cracks which had opened along the front wall of the inside of the front wall of the basement had previously been pointed up. Something that was obvious to me after he showed me, but which I had never noticed before.

Q. Let me just establish this for the record. Those I-beams that you have mentioned, were they put in by you?

A. They were not put in by me. They were there.

Q. Did you have any pointing up on cracks filled in prior to the time these visits—

A. I absolutely had nothing done to the house of this kind in any way.

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[fol. 29] CROSS-EXAMINATION

BY MR. FITZGERALD:

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[fol. 30] Q. And these photographs which are in evidence show the condition of the house today, does it not?

A. That's right. These were taken last, last Sunday, I think.

Q. Can you point out anything in these photographs which was present in this condition on or before June the 2nd of 1957?

A. Of my own knowledge that they were present?

Q. Yes.

A. No, indeed.

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Q. Uh-huh. Now when you went to the house, when was the first time you saw that house?

A. First time I saw it, March 14, 1957.

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[fol. 31] A. After the 14th of March the only time I was inside the house before the 2nd of July was on about the 15th of June after the contract had been gone into effect.

• • •

Q. Were the grounds well gardened, appropriately planted?

A. I don't quite know what you mean by that.

Q. Were they landscaped? Did they have appropriate planning on the grounds?

A. We didn't think they were appropriate. They were landscaped. The house was completely covered with ivy, almost completely.

[fol. 32] Q. It was almost completely covered with ivy?

A. That's right.

Q. Where was the ivy not covering the house?

A. Well, there was, it was no ivy obviously—well, not obviously, but right over the front door. I think there was no ivy on the side of the sun parlor, and there may not have been ivy, I am quite certain there was not above the sun parlor on the east wall of the house, but except for that most of the house was covered with ivy.

Q. And in March of 1957 or the spring, several months of the spring of 1957, most of the areas where are covered by these photographs would have been covered, is that not correct?

A. Except for the areas I have just mentioned.

Q. I see, and you have since removed all that ivy?

A. A large part of it.

Q. I see.

A. It had to be removed so that we could point up the cracks.

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[fol. 33] Q. Tell me the names of all the friends you took to the house.

A. I took Mr. Latto to the house. I took Stanley Segal to the house. • • •

• • • •

Q. And did you have any conversation about the house with Mr. Segal?

A. Yes, I did.

Q. What was that?

A. We both, Mr. Segal went with me, I'm quite sure, on the day which we took title and we both commented upon high cleanly condition the house was in. He and I both noted pointed-up crack on the east wall of the basement and the crack over the front door between the front door and the window which is above it on the front wall of the house. I said to him and I assumed that this was in early settlement which had been remedied. That was the extent of the conversation.

Q. And was there any dampness or water in the basement?

A. No, none whatsoever.

Q. And did you talk with Colonel Ormquist about the [fol. 34] condition of the basement?

A. I remember asking him whether the basement got damp or whether it leaked, and he told me no. And I

could see that the basement was painted with Sta-Dri and he told me that he would leave partially filled can of Sta-Dri with the house when he left?

Q. Did he say that he had done any work on the house in connection with what we have just talked about, the basement?

A. I have the impression that he painted the basement with Sta-Dri, but if he told me that, that is all he told me about whether he did any work on the house himself.

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[fol. 35] • • • •

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[fol. 36] BERNARD F. LOCRAFT

was called as a witness by counsel on behalf of the plaintiffs and, having been first duly sworn, was examined and testified as follows:

DIRECT EXAMINATION

BY MR. LATTO:

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Q. And what is your profession?

A. I am a civil engineer.

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[fol. 37] • • • •

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[fol. 38] Q. Were you retained by Mr. Neustadt sometime in August, 1957, to advise him as to how he might meet the problems he's just finished describing?

[fol. 39] A. Why I was—I never knew Mr. Neustadt before, but he did retain me at that time.

Q. And did you personally make an examination of the house?

A. I personally visited the house on August 19, 1957, and examined it very carefully.

Q. Did you examine it at any other time?

A. I went to the house on several subsequent occasions during the course of my advice to Mr. Neustadt.

Q. Can you describe to the Court, give us a general description of the condition of the house as you found it on those days?

A. I found the house at 1408 Oakcrest Drive to be a two-story and basement, brick and cinder block, single-family home. I noticed the yard had several large trees in it, particularly near the front of the house. The house is located on the southerly side of Oakcrest Drive, several blocks east of the Fairlington subdivision. The yard around the house was relatively at and level at the house, but the terrain to the south and west of the house drained towards Mr. Neustadt's home without provision being made at the building to drain the water away from the walls of the house. I examined the exterior of the home and on the north or front of the house I noticed a vertical crack over the front door running up to about the second [fol. 40] floor level, and then easterly to the northeast corner of the building. At the, about the first floor level of the house I noticed a horizontal crack running towards the west corner of the house, northwest corner of the house. This crack was such that the basement wall had been pushed into the basement about an inch. That crack had been pointed up at some time. Previously.

On the east side of the house is a one-story sun parlor or sun porch. That sun parlor had a vertical crack at its junction with the main house, running from the ground up to the roof. On the south or rear of the house was a vertical crack over the head of the east window and also a horizontal crack near the kitchen door. On the west side of the house there was a horizontal crack about one-quarter of an inch wide at the first floor line, just about ground level, at the southwest corner.

Q. Let me interrupt you one moment. There has been some testimony about ivy which had covered a good part of the front wall of this house, the north wall. Had that ivy been removed or was it still present at the time of your examination?

A. Most of the walls of the house were covered with ivy, but these cracks were perfectly obvious to me.

Q. Were there any indications in any of these cracks that you have just referred to of having been previously pointed up?

[fol. 41] A. Yes, the crack in the front wall which was near the ground level where the basement wall had been pushed in about an inch had been pointed prior to my visit.

In the basement of the house I observed that the basement walls were 12 inches thick, of cinder block and that there were a number of cracks in those basement walls.

In the east wall there was a diagonal crack which had been pointed up. I could see that that crack had been about an inch and a half wide and on occasion of my visit the crack had again opened about an additional three-eights of an inch. It was a fine crack in the south wall over the laundry tub. There was a horizontal and vertical and diagonal crack in the west wall of the house in the basement. That crack ran from the floor to the ceiling before it stopped. And the north wall or front wall of the house there was a crack three-eigths of an inch wide about four feet three inches above the floor running the full width of the north wall. The basement floor of the cellar was badly cracked and out of level.

I observed two steel I-beam posts or columns placed near the north wall under the floor beams.

Q. Were you able to tell whether those columns were part of the original construction of the house or they had been added at a subsequent time?

A. From my knowledge of the situation I would say [fol. 42] they had been added after the building had been built. When, I don't know, but they were an afterthought. I then went up on the first floor and in the kitchen. There were cracks over the kitchen door and between the door from the kitchen to the dining room; in the dining room the crack showed over the door to the back into the kitchen, and also at the arch doorway going into the entrance hall.

There were also cracks in the ceiling, the dining room. In the entrance hall there were fine cracks over the arched doorway, both back into the dining room and leading over to the living room. The crack at the living room was clean and fresh. In the living room there were cracks over the arched doorway back into the entrance hall.

There was a crack over the doorway leading into the sun parlor. That crack was a wide crack with plaster

fallen from it. It was clean and fresh. I observed that the floor of the living room had a decided slope towards the north or front of the house and that the wood flooring of the living room had pulled away from the north wall about three-eights of an inch.

Q. I am not sure I follow that.

A. The flooring at the front of the house had been, was separated from the north wall by about three-eighths of an inch.

Q. You mean just a gap between the floor and the wall?

[fol. 43] Yes.

Q. I see.

A. I went into the sun parlor and observed the floor of the sun parlor sloping. The doors to the closets in that particular section of the house didn't close, didn't stay closed.

I went up on the second floor and observed cracks going up the stairway. I observed while no tile was broken in the bath, I observed that there were cracks over the head of the door to the hallway, and the northwest bedroom there was a fresh crack across the ceiling, running clear across the room. The floor was sloping towards the north of the house, towards the front. In the northeast bedroom there was a similar situation obtained. And the doors to the closets upstairs did not stay closed, either.

Q. Now did you attempt to devise a plan by which the condition you have just described could be remedied?

A. I investigated the records of the Building Department here in Alexandria to see if anything had been noted during the course of construction, and other than the normal remarks I learned nothing particular from that inspection.

Q. Did you make any investigation of soil near the house or under it?

A. I had one of my men drill an auger hole through a hole in the basement floor near the northeast corner of [fol. 44] the basement down into the soil below and I observed that the basement floor had been placed on a cinder fill, that that cinder fill had water in it. I further observed that the clay, that there was clay under the basement floor and that this clay when it was wet as it was became plastic and pliable.

I had my men establish level marks around the inside of the basement walls and from time to time observed readings on those marks to detect whether or not the building was moving. I also employed a strain gauge across it, at points across the cracks in the basement walls to determine whether or not those were moving, and after several months of observation during which time I did observe that the building was breathing and moving which investigation indicated to me that there was no evident indication that the building would collapse or fall down around people's heads, I suggest that we stop that type of investigation, patch up the conditions and live with it as best they could.

Q. Do you think this foundation could be fixed up so that there would be a reasonable guarantee that this wouldn't happen again in the future?

A. I tried to devise some sensible way of underpinning this building, but I did not come up with any economically sound.

Q. What kind do you think it would require, assuming you were not concerned for the moment about costs?

[fol. 45] A. I would require that either pipe fills or some sort of a post or column arrangement be placed at intervals under the basement walls down to a good, firm, unyielding material, perhaps 15, 20 feet below the surface.

Q. Is there any other method that might be devised that would accomplish a similar thing?

A. A general underpinning of the entire walls by placing a wider-spread footing, tying the whole foundation together as a mat might be employed, but neither of these, I guess, are economically practical. Just too expensive.

Q. Did you make any recommendation with respect to the grading of the lot?

A. Yes, it seemed to me that if we could arrest the surface water from settling around the house we could eliminate a great deal of the water under the building. With that in mind we prepared a plan showing several ways, troughs around the building which would lead the water and collect the water before it hit the building and lead it away from the house. That work was done by Mr. Neustadt.

Q. Is that a fairly substantial job?

A. It was. It took quite a little while, and to a great extent I think it has helped to take the water away from under the building, but there is still water under the building.

Q. The second of these two possibilities, pouring spread footings and typing them in, I am not quite sure I under- [fol. 46] stand that. I have heard of pouring additional footings under a house when you have settlement problems. Is that all you're talking about, or is it something more?

A. Well, it is in a few words, it is just the footings that are under the house today are two feet wide. I learned from the record here in the Alexandria Building Department. It would be necessary to have footings that were several feet wide, maybe four or five feet wide, maybe wider, to spread the load safely on this soft clay.

Q. And that would have to be throughout the foundation?

A. That would be done throughout and would be done in sections four feet at a time around the entire perimeter of the house and would be time-consuming job as well as an expensive one.

Q. I see.

Mr. Locraft, on the basis of your examination of the premises in August which you have just described to us, are you able to make an informed judgment as to whether there must have been evidences in mid-March of 1957 either of current settlement and structural damage or of indications that there was something to be concerned about in this area?

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[fol. 47] Q. Let me ask you specifically with respect to some of the things you mentioned earlier describing the house, you mentioned the place where there was a large crack that had been pointed up along the floor, first floor line which had had a transverse movement of about an inch.

A. That's correct.

Q. Are you able to say whether that crack had been present in March of 1957, from your examination in August?

[fol. 48] A. I would, of course I was not there in March, but from what I saw in August that crack had been there a long, a long time.

Q. How about this displacement of about an inch that you described, could that have taken place in this five-months period, or is that something takes place over a longer period of time?

A. No, that had been there a long period of time.

* * * *

[fol. 49] CROSS-EXAMINATION

BY MR. FITZGERALD:

Q. Mr. Locraft, did I understand you to say that the parlor floor sloped, too, sun parlor?

A. Yes, sir.

Q. And were you able to determine what might have caused that?

A. The settlement of the north wall across the entire house contributed to the settling of the floor.

Q. Was the sun parlor enclosed?

A. Partially enclosed. It is enclosed with, like a, with glass or something, make it an enclosed porch.

Q. Was it enclosed with brick at all?

A. Brick piers, posts of that nature.

Q. And you advised them to point up the cracks and live with it as best they could; is that correct?

A. In a few words that is it, sir.

Q. Can that be done? Can you conceal the cracks with [fol. 50] some success by pointing them up, painting over them?

A. Only temporarily. You can conceal the cracks, but they will reopen again when you do not know, maybe the next day, maybe the next couple of weeks, but they will continue to reopen.

Q. And if you do try to live with it, point them up, paint over them, you can keep them concealed temporarily?

A. Yes, sir.

* * * *

[fol. 51] Let me ask you, have you any reason which you could say as to why this defect did not appear some-

[fol. 52] time in 1945 or '46, five years after the house was built, or 1951, ten years after the house was built?

A. In my observation, as I went into the basement and looking around the outside, I would say those cracks could conceivably have been even of that age, maybe older.

Q. Maybe even older?

A. Yes.

Q. And if they were of that age, there'd been no guarantee that they were continuing or they might have just been original settlements; is that correct?

A. There again, sir, your're on the wrong premise. You do not build houses expecting them to settle.

Q. Well, I am trying to segregate these things, and if we were to look at the crack alone, not knowing what the house was built on, it is your testimony that it might have been there as much as ten years and might not be likely to further its condition?

A. It may have been there as much as ten years, but the fact that it was not likely to continue is not according to the fact, because I saw the freshly opened—

Q. Well, the likelihood or lack of likelihood of its continuing would be dependent upon what the house was built on, not it on, on the appearance of the pointed-up crack?

A. Yes, that's a good way to put it.

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[fol. 53] * * * *

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[fol. 54] HARRISON C. JACOBS

was called as a witness by counsel on behalf of the plaintiffs and, having been first duly sworn, was examined and testified as follows:

DIRECT EXAMINATION

BY MR. LATTO:

Q. Would you state your full name and address, Mr. Jacobs?

A. Harrison C. Jacobs. Business or home?

Q. Well, where are you employed?

A. 333 Third Street, Washington, D. C.

Q. And with whom?
A. I am with the Federal Housing Administration.
Q. What is your position with the F.H.A.?
A. Supervisor of inspectors.

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[fol. 55] Q. I'd like to shorten this as much as I can, Mr. Jacobs. Were you in the courtroom when Mr. Neustadt testified?
A. Yes, sir.
Q. And did you hear his testimony with respect to a visit or a number of visits that you made to his house?
A. Yes, sir.
Q. In July or possibly early August of 1957. He testified also that you told him that in your opinion a bad mistake had been made on the part of the F.H.A.; was his testimony accurate in that you did make such a statement to him?
A. I am not altogether sure about the F.H.A. part, but I realize that a mistake had been made of some nature, and that is the reason I advised him to enumerate each of the items that we discussed and then inform Mr. Elliott, our chief underwriter.
Q. What was the nature of the mistake that you considered had been made?
A. Well, it's kind of rehash, but cracks in the front, bad drainage, the apparent wrenching of the sun parlor from the house, and the big subsidence crack in the basement, plus the crack that the right-hand side or east wall, [fol. 56] I believe it is, in the basement, and then the large one in the front wall.
Q. Now, was it your view at the time that you inspected the house, and is it your opinion today that these evidences that you have just mentioned must have existed in March of 1957 when the inspection was made?
A. Without question; yes, sir.
Q. Was that your opinion?
A. Yes, sir.
Q. And it is your opinion now?
A. Yes, sir.

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[fols. 57-60] • • • •

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[fol. 61] CROSS-EXAMINATION

BY MR. FITZGERALD:

* * * *

Q. Now in your experience is it possible to point up [fol. 62] and paint over cracks which are the result of settling of foundation?

A. It's been my experience that you can do that, but if the original cause still prevails quite often you will get the reopening of those cracks.

Q. They will reopen, but can they be concealed temporarily by pointing and painting?

A. Yes, s .

Q. For approximately how long could a serious crack, and let me explain "serious" crack by saying that I mean a crack which comes from a serious cause, but maybe no wider than an ordinary crack in the building be covered, painted over and concealed by painting and pointing? How long a period could you conceal such a thing before it would reopen, approximately?

A. Hm-m, a real serious crack I venture to say would reopen within ninety days.

Q. Within ninety days?

A. Yes, sir.

Q. And in your experience do you ever come upon cracks which have been pointed and painted which are not the result of serious flaws in the house?

A. Yes, sir.

Q. Might there be a crack in this courtroom wall which is not the result of a serious failure?

A. Yes, sir.

[fol. 63] Q. Might it be pointed and painted?

A. Yes, sir, and never show up.

Q. What kind of cracks are those?

A. We term those shrinkage cracks.

Q. Shrinkage cracks?

A. Yes, sir.

Q. And if a crack has been pointed and painted, after it has been pointed and painted, is there any way for a person not experienced in architectural field to know what kind of a crack it is?

A. No, he wouldn't know, not in the architectural field; no, sir.

MR. FITZGERALD: That is all.

MR. LATTO: Let me ask you about the particular crack in this house. There has been some testimony about a crack in the basement on the east wall. That is the wall underneath the sun parlor, or which had been pointed up and painted, would that crack be observable, or could that crack have been covered up by paint, in your judgment?

THE WITNESS: By observing that crack that had been patched, I'd say offhand in my own opinion and experience that it had been a fairly wide crack and it wouldn't be too hard to tell.

BY MR. LATTO:

[fol. 64] Q. How about the crack we mentioned on the outside of the house on the first floor line where that had been, this transverse movement, was that something that could have been readily concealed by point and, pointing and painting?

A. No, sir.

Q. Was the ivy covering the front wall of the house at the time you saw it?

A. To a certain extent; yes, sir.

Q. Have you seen the picture of the house that is in evidence? This is the way it looked, or was there much more ivy on it at the time?

A. If I am not mistaken, there was a little more ivy on that.

Q. And did that interfere with your ability to find these cracks that you have mentioned?

A. No, sir.

Q. How about these I-beams in the basement, did you notice them?

A. Yes, sir.

Q. And what did they indicate to you?

A. That they'd been there quite some time. In other words, the installation of those hadn't been too recent.

Q. Was it evident that this was not part of the original construction of the house?

A. Oh, yes, sir.

[fol. 65] Q. If you were making an inspection and appraisal of the house, would the presence of I-beams of that sort indicate the need to you of a thoroughly careful examination with respect to settlement problems?

A. Yes, sir.

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[fol. 66] THOMAS CUNNINGHAM BARRINGER

was called as a witness by counsel on behalf of the plaintiffs and, having been first duly sworn, was examined and testified as follows:

DIRECT EXAMINATION

BY MR. LATTO:

Q. Would you state your full name, please, Mr. Barringer.

A. Thomas Cunningham Barringer, 301 Harvey Road, McLean, Virginia, Director of F.H.A., District of Columbia Insuring Office.

* * * * *

[fol. 67] Q. So that it will be perfectly clear to this, I know that are many programs that undertake to administer, all of my questions will be directed to the single question of the activity of the F.H.A. in connection with the insurance of mortgages on single-family dwellings, and that would be under, I guess, it is Title 2203 of the statute. Is that reference correct?

A. That's right.

Q. And the functions of the F.H.A. under that section of the National Housing Act include insurance of both new construction and old construction, is that right?

A. That's right.

Q. My questions will be directed only to the insurance of mortgages written on houses already constructed.

Can you tell us briefly what the principal division is in your office that are concerned with the function of the insurance of mortgages on single-family dwellings of this type?

A. Well, of course, there is the administrative side of the office that does the receiving of the applications.

There is the architectural section that on existing houses only, called in or making repair inspections, or for consultation on difficult cases. There is the evaluation section that takes the application of the property, the description, that goes out and makes the evaluation and [fol. 68] turns in the report. There is the mortgage credit section that passes on the purchaser after the appraisal has been made, if it's an application for a firm commitment, as we call them.

Q. Let me try to do this in a chronological way. Suppose, take the case of a person who owns a house and is interested in selling it, and believes that he may be able to get a better price or sell it more readily if he can assist in arranging for F.H.A. insurance on the financing that will be employed in the sale of a house, what should he do or what does he do if he reaches such a decision, or may he do anything, first of all?

A. He would have to go to some mortgagee, either himself, or through his broker, and make application for a conditional commitment, assuming that the purchaser is unknown.

Q. This is before he's even heard of a purchaser?

A. That's correct.

Q. He can have an application filed on his behalf or on behalf of the mortgagee for what you refer to as a conditional commitment?

A. That's right.

Q. What does the term conditional in that respect mean?

A. Well, conditional commitment means that we will appraise the house and state the amount of loan that we are willing to insure to an unknown borrower or unknown purchaser, and this conditional commitment would [fol. 69] be converted into a firm commitment if we accept the borrower as being qualified to carry the mortgage.

Q. Let's hold the borrower for a minute. What happens when this application is filed with the F.H.A. when it is received by you, what steps are taken in your office?

A. It is logged in. It's given a number, and it goes into the evaluation section and is assigned to an appraiser to go out and take a look at the property. He returns and make up his appraisal report, and then it is reviewed.

Q. Before that, let me ask this, on what form would his appraisal report be made?

A. Form 2710.

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[fol. 70] Q. • • •. Suppose that the contract for the purchase of a house had been made and as part of the conditions in that contract it was required that F.H.A. insurance in a certain amount be available, would there [fol. 71] be any different practice so far as the application for mortgage insurance is concerned? How would the application for mortgage insurance be filed in that case?

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A. Well, then customarily the buyer of the house goes to a mortgagee and requests that they file an application on his behalf for an F.H.A. commitment.

Q. What would be the reason for someone who owns a house to have such an application filed before he even knows who he might sell this house to?

A. Because he wants to ascertain what he thinks F.H.A. thinks the house is worth, and what amount of mortgage would be obtainable on his house under F.H.A. insurance feature.

Q. So that discussing the sale—

A. To a—in event that a suitable purchaser arrived, it is a time-saving facility.

Q. In discussing the possible sale with a future purchaser he can inform him that he's had the house ap- [fol. 72] praised, that a certain mortgage, if he can find a lender, will be insured by the F.H.A.?

A. Find a purchaser.

Q. Upon the proper controls in respect to the credit of the purchaser.

Now let me return to this form. This I take it is not the application for insurance that we are discussing; is that right?

A. No, this is an internal form of F.H.A. prepared by various sections of the office where they are effecting, they are in the process, where they contact the processing of the case.

Q. And a considerable portion of this form is completed by the person who makes the appraisal, the inspection and appraisal; is that correct?

A. Yes.

Q. Now let me come back to this item 31 which reads, Estimated cost of repairs, improvement proposed, and a blank for a certain number of dollars to be entered or required and a blank for a certain number of dollars to be added. What is the function of that particular entry on this form, and who was the person who would complete that particular line?

A. Under this form, performs a dual purpose. If it was new construction, then all of the architectural section would be filled in completely by the architectural section. [fol. 73] Q. Yes. You understand my yes is directed to old structure

A. If an evaluator and appraiser is looking at a piece of property in "as is" condition in order to arrive at his value he has to estimate the replacement cost of that property, and he has to take into account certain factors, but the value may not exceed the replacement cost. Having arrived at that figure, it is purely his judgment based on the experience data that we have as to size of the house, amenities. He then proceeds to make his appraisal based on the other factors involved, location, community, physical appearance, security, and what-have-you.

Q. Now this, you haven't yet mentioned the word repairs which appears on item 31. I am trying to discover what the function of that line is.

A. Well, he may look at the existing house and think that certain repairs should be done, or he may or may not consider them necessary, and he's taking them into his value when he made his appraisal.

Q. Let me come at this another way.

Do you have a copy of F.H.A. letter No. 1272 of August 11, 1952, before you?

A. I do.

Q. Would you turn to page, well—and does this document contain instructions to the people who are concerned [fol. 74] with the architectural processing of this Form 2017?

A. That is correct.

Q. Would you turn to page 6, down at the bottom of the page, you will find item 31. If I read that, since it is very brief. It says, Estimated cost of repairs or improvements proposed or required, in existing construction cases only, enter separately in the spaces provided the estimated cost of any repairs or improvements, a, parenthesis proposed by the mortgagor and b, in parenthesis, any additional repairs or improvements required by F.H.A. as essential to eligibility.

Now I want to direct your attention to this last phrase which begins with parenthetical b, in parenthesis, would you explain to the Court what is meant by additional repairs or improvements required as essential to eligibility?

A. Well, it is possible that we will see an existing house and we figure that, that if the certain improvement is made like new gutters or painting of the exterior or myriad of improvements that might take place to the property, we will give full value to the house, provided they are made the conditions of our commitment, that they be done.

Q. Now when this says essential to eligibility, does that mean in the event these repairs are not made that the F.H.A. will refuse to insure the property?

A. If we made the requirement, then we will not insure.

Q. Then you do have a practice of, in certain cases, of [fol. 75] imposing requirements before you will issue mortgage insurance?

A. Definitely.

Q. Can you tell us the kind of the situations in which those requirements will be imposed?

Well, for one thing the question of termite damage, been mentioned to the Court before, what happens if your inspector notices a serious evidence of termite damage in the house which is the subject of an application for mortgage insurance?

A. Well, if an appraiser sees evidence of termite, we make a condition on the commitment that a reputable firm proceed to cure this situation and give a five-year guarantee, and such evidence of that guarantee and working having been done is submitted with the papers to F.H.A. at the time of our insurance endorsement that the con-

dition has been complied with. An appraise may also go to an older house in an area that he suspects might have termites and see no evidence whatsoever but still require a lesser type.

Q. Yes, I understand.

A. Of examination by a competent exterminator, just to be sure that it is; it's a matter of judgment, wants to be certain.

* * * * *

[fol. 76] Q. Now suppose an inspector made an appraisal of the house and discovered evidence of serious settling and it was his judgment that there was danger, continued settling in the near future, what would these instructions require him to do?

A. Well, if the appraiser observed a serious settlement condition, he would, depending on his own experience, either make it a requirement for correction on the basis of what he knew, or he may suspend his appraisal operation and request a review by an architectural man in the office to determine the extent of the condition.

Q. Now suppose he did the latter and it was the same opinion, his opinion was shared by the man in the architectural section, namely, that there had been serious set-
[fol. 77] tling in this house and there was serious danger of continued settling in the uncertain future but a definite probability of continued settlement, what would then take place?

A. Well, he could reject it, recommend rejection of the application, and usually with the statement that it would be economically unfeasible to correct.

Q. Is it considered part of the function of the appraisers to determine whether there are conditions of this sort, termite damage, structural defect, which might make a particular property ineligible for F.H.A. insurance, to consider that as part of the functions of the appraiser?

A. That is definitely the part of the appraiser. He's an employee of F.H.A. and he'd look at the physical security from our point of view, and I suppose if he sees conditions that are detrimental to our security he is supposed to report them and to make such recommendations. That is in his judgment. It is a matter of judgment.

Q. And they would be noted on this form that we have been discussing?

A. They would be, if he saw them.

• • • •

[fol. 78] • • • •

• • • •

[fol. 79] CROSS EXAMINATION

BY MR. FITZGERALD:

Q. Is the purpose of the F.H.A. conditional commitment when the buyer is yet unknown, is it the purpose of that commitment, so the seller can use that as a sale point in talking with prospective purchasers?

A. Well, that's one of the uses. It is not the--

Q. Is that the F.H.A.'s purpose?

A. The F.H.A.'s purpose is to honor the request for an [fol. 80] appraisal. What use the buyers put it to we have no control over. He may want it for his own curiosity, for purposes of sale, determining many other factors, but so far as F.H.A. is concerned that is where it is most frequently used by many people.

Q. In the question which was asked you about termite damage, if an appraiser saw nothing to indicate to him that there was a presence of termites, is he required in each and every case to make a detailed inspection, sampling of timber, to find out whether or not they are present?

A. No.

Q. What is the duty of an appraiser as to the appearance of a house with regard to detailed inspections of what the appearance might not reveal, that is, latent or hidden qualities or defects?

A. Well, an appraiser may, it is a matter of experience and judgment, he determines the house in its "as is" condition, he finds obsolescence which has nothing to do with the latent defects. Ordinarily he may see a furnace in the summertime and he gives the house a full value for having an operating furnace, but he does not attempt to run it or check it other than the fact that he assumes that it is in working condition.

Q. Is that what he is required to do, or he is entitled to take his experiences at face value?

A. That's right. A dry cellar at the time of his in- [fol. 81] spection is supposed to be a dry cellar. May subsequently be quite different.

Q. That is all.

THE COURT: Mr. Barringer, in this particular instance who made the application for the insurance that led to this appraisal; do you know that?

• • • •

THE WITNESS: • • •

In answer to your question, the owner of the property requested an appraisal or conditional commitment on the property before the purchaser came into the picture.

THE COURT: Well; did the purchaser at any time [fol. 82] come into the picture as far as F.H.A. insurance is concerned?

THE WITNESS: Yes, subsequently having entered into a contract to buy the house, he filed through Thomas J. Fisher and Company, the mortgagee in Washington for approval of himself as the purchaser, that is being qualified to assume the mortgage that we had agreed to insure on the previous commitment.

THE COURT: Well—

THE WITNESS: We did accept him as the mortgagor and endorsed the note after settlement, and it is now an F.H.A.-insuranced note.

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[fols. 83-84] • • • •

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[fol. 85] MR. FITZGERALD: Put in 2710, Plaintiffs' Exhibit No. 12, which is Form 2710. It's introduced into evidence. 2017, introduced in evidence, in blank, is that given to the purchaser or something else?

THE WITNESS: No, at the time that we issue the commitment and send it to the mortgagee we accompany it with a statement of F.H.A. appraisal Form 2562 which shows what, also shows on the commitment itself, the F.H.A. appraised value. The forms for the purpose of [fol. 86] the mortgagee getting to the home owner or the

seller of the property a piece of paper that gives him the appraisal in advance of his entering into a contract. If he does not enter into a contract, he fills out the lower part of the form which amends the contract that he may eventually sign.

BY MR. FITZGERALD:

Q. Now that advice to him from the F.H.A., does that say anything about the house, such as its grounds, its building, or does it describe it in any way, or have anything on it with reference to question 30 and 31 which we have gone into briefly about required repairs or improvements, anything like that on it?

A. Nothing at all. It only has the dollar value of our appraisal, and specifically says the F.H.A. appraised value does not establish the sales price.

Q. That is all.

BY MR. LATTO:

Q. Mr. Barringer, suppose I had entered into a contract which was conditioned on F.H.A. insurance in a certain amount being available for me, to be required to complete that contract and it had been determined by the F.H.A. that this particular property was ineligible for any reason whatever for the mortgage insurance, what would happen at that point? Would this information come to the attention of the purchaser and the seller of the house? [fol. 87] A. Very definitely. We would issue a form known as report on application which in various types of language says a reject.

Q. And this information would come back to the people concerned?

A. That's correct.

MR. FITZGERALD: That's all.

(The witness stepped down.)

Thereupon,

RANDALL J. HICKS

was called as a witness by counsel on behalf of the plaintiffs and, having been first duly sworn, was examined and testified as follows:

DIRECT EXAMINATION

BY MR. LATTO:

Q. Would you give us your full name, please, Mr. Hicks.
A. Randall J. Hicks.
Q. What is your business address?
A. 3706 Mount Vernon Avenue, Alexandria, Virginia.
Q. And what is your business?
A. Real estate broker.
Q. How long have you been engaged in this business?
A. Fifteen years.
Q. Have you in the course of your occupation as a real estate broker done very much appraising of single-family [fol. 88] dwellings?
A. In the last twelve years I have done a good bit of appraisal.
Q. Tell us something about the nature of your experience in this area.
A. Of course, the majority of my appraising is residential property insofar as my business is concerned. I do condemnation appraising. I do estate appraising. I do appraising for the courts, various types and nature.
Q. Did you in October of 1957 at my request furnish me with an appraisal of the fair market value of property at 1408 Oakcrest Drive in Alexandria?
A. I have a report of such an appraisal to Mr. Neustadt on October 31, 1957.

• • • •

Q. And can you tell the Court what your opinion was as to the fair market value of this property?
A. Well, first I'd like to preface my remarks by saying [fol. 89] that a fair market value of a house in the condition this was at that time had a good deal of guesswork based on experience because in appraising, to do it accurately and scientifically, you not only have to take in certain factors, but additionally you should have comparables

to make sure to check out your information—is correct—and on this particular house I knew of no comparables and, therefore, I could not arrive at any accurate value based on comparables, so I had to do it on the basis of estimated repair which would bring it up to its condition which preceded it, before this settlement took place.

At that time I estimated the value of the property at thirteen thousand, figuring it would take the difference between that and $24,000 odd to put it in good condition, and there again it was more or less of an estimate based on observation because I could get no one to give me a firm bid on the condition it was in.

Q. Let me ask you this. Do you think the market value was precisely equal to the difference between what it would be worth if it were in perfect condition and what it was worth in the condition in which you saw it? Would the difference of repairing the house be the sole difference in the market value? I don't know if I made that question clear.

Let me rephrase it, if I may.

Would you say that the market value of the house in [fol. 90] the condition in which you saw it would be determined by simply subtracting from what its fair market value would have been had it been in perfect condition, the cost of repairing, the damage, that you saw?

A. Well, that is just simply one approach. Of course, there is no way for anyone to tell, at least no way for me to tell what someone would come along and offer cash for that house in that same condition. To get someone to do that, I think they would do just what I did. They first find on it as accurately as possible what it would cost to put it in A-1 condition, and then you'd subtract that from what the market value would be in A-1 condition, and that, presumably, would be what it's worth in its present condition.

Q. Well, the things I am struggling with, is this—suppose we take two houses which are identical in the same neighborhood and they are identical except for the fact that one of them has a serious structural defect of some kind. If I were a possible purchaser of one of these two houses, do you think that I would be as willing to pay $5,000 less for the house that was in poor condition if I

thought it would cost me $5,000 to repair it, or would I prefer to have the house that was in good condition without paying anything to repair it?

A. I don't think I can give you an honest answer there because you are asking me to tell you what someone else would do. Now based on my experience, people, if a [fol. 91] house is in good condition at the time they purchase it, they don't quibble about what it might cost to put it in good repair in case it becomes necessary to repair it later, so I couldn't accurately answer your question in that respect.

Q. Well, let me ask you this. I am reading from the appraisal report that you submitted to Mr. Neustadt, October 31, and you said any prospective purchaser would obviously prefer to purchase a substantially similar house in good condition at a price equal to its market value rather than pay a price for this property equal to its former market value, reduced by the probable cost of correcting the present condition.

Now that is what I had in mind.

A. That was an opinion that, therefore, I had reduced the price of the present market value to that extent. I mean the thirteen thousand took into consideration that that would, might happen.

* * * *

[fols. 92-123] * * * *

* * * *

[fol. 124] MRS. R. H. HUBBARD

was called as a witness by counsel on behalf of the Government and, having been first duly sworn, was examined and testified as follows:

* * * *

[fols. 125-129] * * * *

* * * *

[fol. 130] CROSS-EXAMINATION

BY MR. LATTO:

Q. Were you here during Mr. Neustadt's testimony?

A. Yes, I was.

Q. He testified to certain conversations with you with respect to the F.H.A. appraisal. Do you recall that testimony?

A. Yes, sir.

Q. At one point he said he testified that after the first F.H.A. appraisal was received, he telephoned you to find out whether that might possibly mean that there was any structural defect in the house. Do you recall that conversation with him?

A. I do recall a conversation but I believe it was with Mrs. Neustadt, but I am sure that one of them called me.

Q. He went on to testify that he was informed by you that it was a practice of the F.H.A. either to refuse to insure a house or to condition their insurance upon a substantial defect being remedied, if there was one. Do you [fol. 131] recall giving him that information?

A. Well, it sounds very much like me because I have firmly believed that.

Q. Now would you say this information about F.H.A. practice is commonly known?

A. Yes, I always believed that the F.H.A. would not insure a loan or on a house that wasn't worth it, and I always thought that was a very excellent yardstick, so I would say that that sounds very much like me.

Q. You don't recall the particular words but you certainly wouldn't deny that you gave him that information?

A. I couldn't deny if Mr. Neustadt said I said that. I would believe I had.

Q. That is all.

MR. FITZGERALD: That is all.

Mr. Wharton.

Thereupon,

HENRY REDWOOD WHARTON, III

was called as a witness by counsel on behalf of the Government and, having been first duly sworn, was examined and testified as follows:

DIRECT EXAMINATION

BY MR. FITZGERALD:

• • • •

[fol. 132] Q. What is your occupation?

A. Real estate.

Q. And in connection with real estate do you do any appraising?

A. I do.

Q. For how long a period have you done so?

A. Well, for fourteen years, as long as I have been in the business.

Q. Have you engaged in any special training or courses to enhance your ability to do appraisal work?

A. Yes. I have taken the American University, both courses in Appraisal I and another Appraisal II. Those are both courses set up by the American Institute of Real Estate Appraisers in Chicago. I passed both of them.

• • • •

[fol. 133] Q. Mr. Wharton, in connection with your physical inspection of the property what do you do?

A. Well, let me start with a definition of appraisal to begin with. It's an estimate of value made by the appraiser, and it has to be made on the basis of his—well, [fol. 134] let me start again.

It is his evaluation based on the observed condition of the property at the time he looks at it.

Q. And in connection with the observed condition of the property do you make a detailed physical inspection?

A. Yes, you do.

Q. And in connection with that physical inspection what did you accept as fact and what do you question and inquire further?

A. Well, an appraiser is not required to be a construction analyst. He just has to take what he sees and appraise it as it is and as he sees it.

Q. There was some testimony the last day of trial about the situation presented by a furnace on a house being appraised on a day like today. What would be the duty of an appraiser there as to the condition of that furnace?

A. Well, I can only go along with Mr. Barringer, who,

of course, is an F.H.A. man. He says that they have to assume that furnace is a working furnace even though they don't see it in operation.

Q. And did I ask you to inquire and for your professional judgment on what the duties of an apprais are in this field?

A. Yes.

Q. And did you consult some research?

A. I certainly did.

[fol. 135] Q. Works or books and other people in the field?

A. I did.

Q. And are you able to tell us about the foundation of a house which is under appraisal, if the appraiser does not detect any noticeable faults in the foundation, whether he is required to look further?

A. Generally I would say not, if everything looks all right. The appraiser is normally expected to be satisfied.

Q. And would it, your judgment be affected in any way by the fact that the house was built some eighteen or sixteen years earlier than the appraisal?

A. Well, age is always a factor in appraisal, have to consider that.

Q. Well, in connection with an appraisal, work, do you sometimes come upon cracks in the wall of a house which have been covered up or pointed up and then painted over?

A. Very frequently.

Q. And ordinarily what do they represent?

A. That is a very general question. I—

Q. Well, do they—

A. Settlement cracks, all kinds of degrees of settlement cracks.

Q. And are there different kinds of cracks, cracks other than settlement cracks?

A. Yes, there's cracks from shrinkage and that sort of [fol. 136] thing.

Q. And in connection with settlement cracks, does that indicate any major structural fault or flaw in the house?

A. Not necessarily. Every house when it is first built is going to have some settlement. Most houses, if they

are properly built, will have most of the settlement in I would say the first eight to ten years of their lives.

. . . . .

[fols. 137-139] . . . . .

. . . . .

[fol. 140] BY MR. FITZGERALD:

Q Mr. Wharton, assuming that any defects which later developed or became evident in the house had been pointed up, including those described by Mr. Locraft, that is the outside defect, and any cracks which can be pointed up and painted were so treated, and that there was, what-[fol. 141] ever, half-inch slope in certain rooms, would you say that it would be the ordinary prudent appraiser would be entitled to assume that that house was structurally sound or had the average structural soundness for the value he was putting on the house?

A. That is a difficult question to answer. Are you saying that if the house were fixed up now and painted up to look—I feel that the house is different, the condition is different now from what it was at the time the F.H.A. appraiser looked at it, quite a bit different.

Q. I am trying to—I think you're stating the Government's position accurately there, and I am trying to extract your expert judgment on the, what the duty of the reasonable and prudent appraiser would have been in March, March 14, on the condition of the house in its decorated condition, and I am trying to give you as an assumption the facts which Mrs. Hubbard and some of the other witnesses testified to as a fresh, clean, redecorated house, including Mr. Locraft, statement about a pointed-up crack on the front wall and the other cracks corrected.

A. Based on the testimony I have heard here, where certainly four people, maybe more, looked at that house at the time of purchase, the purchase was made, I think that the appraiser did do the job he was supposed to do. Certainly if these people had any doubts, they should have had it looked into at the time. But they were all satisfied [fol. 142] from what they saw that it was all right.

. . . . .

DUPLICATE

[fol. 143] GOVERNMENT'S EXHIBIT No. 2

To be prepared in duplicate and accompany the commitment; both original and copy to be delivered to purchaser; the duplicate copy to be signed by purchaser and delivered to FHA by mortgagee with ☐ Application for conversion or change of borrower. ☒ Closing instruments.

FEDERAL HOUSING ADMINISTRATION

STATEMENT OF FHA APPRAISAL

Case No. 54-112923

In compliance with Section 226 of the National Housing Act, as amended, the Federal Housing Commissioner has appraised the property identified by the captioned case number, and for mortgage insurance purposes has placed an FHA-appraised value of $22,750 on such property as of the date of this statement. (*The FHA appraised value does not establish sales price.*) This statement of FHA appraisal does not indicate that the Federal Housing Commissioner has approved a purchaser of the property as a mortgagor for an FHA-insured mortgage, nor does it indicate the maximum amount of any insured mortgage that would be approved for an individual mortgagor.

Date—June 4, 1957

J. C. Tracy Authorized Agent

MORTGAGOR'S CERTIFICATION

Check applicable box—

☐ Sale of property not involved; dwelling was constructed by the undersigned for his own occupancy.

☐ The original of this statement was given to me prior to my signing any contract to purchase the above-identified property.

☒ The FHA Statement of Appraisal value was not received by me prior to my signing the contract to pur-

chase, but the contract to purchase contained the following language:

"It is expressly agreed that, notwithstanding any other provisions of this contract, the purchaser shall not be obligated to complete the purchase of the property described herein or to incur any penalty by forfeiture of earnest money deposits or otherwise unless the seller has delivered to the purchaser a written statement issued by the Federal Housing Commissioner setting forth the appraised value of the property for mortgage insurance purposes of not less than $22,750.00, which statement the seller hereby agrees to deliver to the purchaser promptly after such appraised value statement is made available to the seller."

"The purchaser shall, however, have the privilege and option of proceeding with the consummation of this contract without regard to the amount of the appraised valuation made by the Federal Housing Commissioner."

Date—July 2nd, 1957.

/s/ Rose-Barbara J. Neustadt

/s/ Stanley S. Neustadt
Purchaser

[fol. 144] PLAINTIFF'S EXHIBIT No. 13

FEDERAL HOUSING ADMINISTRATION
Washington 25, D. C.

Architectural Analysis
Arch. (4)

August 11, 1952
No. 1272
Supersedes No. 889

TO: DIRECTORS OF ALL FIELD OFFICES

SUBJECT: UNDERWRITING REPORT—FORM 2017—REVISED MARCH 1952—ARCHITECTURAL PROCESSING

This letter with the instructions herein set forth supersedes Letter No. 889 which shall be retained in the Architectural Section until the current supply of the Underwriting Report, Form 2017 has become depleted and the March 1952 revision is placed in use. The instructions hereinafter set forth shall then be made effective.

Underwriting Report, Form 2017, is used in reporting the results of processing all applications for mortgage insurance involving Amenity Income Properties. The Underwriting Report is divided into three parts, namely, Architectural Report, Valuation Report and Mortgage Credit Report. The instructions in this letter pertain to the preparation of the Architectural Report by the Architectural Section.

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[fol. 145] *31. Estimated Cost of Repairs or Improvements Proposed or Required:* In existing construction cases only, enter separately in the spaces provided the estimated cost of any repairs or improvements (a) proposed by the mortgagor and (b) any additional repairs or improvements required by FHA as essential to eligibility.

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[fol. 145A] PLAINTIFF'S EXHIBIT 15

FEDERAL HOUSING ADMINISTRATION
Washington 25, D. C.

February 10, 1955

Operations Letter
No. 121

To: DIRECTORS OF ALL FIELD OFFICES

SUBJECT: STATEMENT OF FHA APPRAISAL—FHA FORM 2562

Section 226 of the National Housing Act, as amended by the Housing Act of 1954, requires that purchasers of FHA insured properties receive a statement of the FHA appraisal prior to execution of the sales contract. The intent and purpose of Section 226 is to give a prospective purchaser of a property informed judgment as to its reasonable value.

To implement Section 226 of the Act and to prevent rejection of cases in which sales contracts were executed prior to filing of application for mortgage insurance, language was provided in FHA Form 2562 which could be used in amending the sales contract. However, there appears to be some misunderstanding as to what is required with respect to the dollar amount which is to be inserted in the amendatory language. It is obvious, of course, that unless a reasonable dollar amount is used in the amendatory language the purchaser does not have the protection intended by the legislation, which is to permit his withdrawal from the contract in the event the FHA valuation is not equal to the amount set forth in the clause.

• • • •

[fol. 146] UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

No. 8071.

UNITED STATES OF AMERICA, APPELLANT,

versus

STANLEY S. NEUSTADT and
ROSE-BARBARA Y. NEUSTADT, APPELLEES.

Appeal from the United States District Court for the Eastern District of Virginia, at Alexandria.
Albert V. Bryan, District Judge.

(Argued May 31, 1960)

OPINION—Filed August 19, 1960.

Before SOPER and BOREMAN, Circuit Judges, and BARKSDALE, District Judge.

Morton Hollander, Attorney, Department of Justice, (George Cochran Doub, Assistant Attorney General, Joseph S. Bambacus, United States Attorney, Samuel D. Slade and William A. Montgomery, Attorneys, Department of Justice, on brief) for Appellant, and Lawrence J. Latto for Appellees.

[fol. 147] SOPER, Circuit Judge:

The question in this case is whether the purchaser of a single residence property covered by a mortgage under § 203(a) of the National Housing Act as amended, 12 U.S.C. § 1709(a), is entitled under the Federal Tort

Claims Act, 28 U.S.C. § 2671 et seq, to recover damages occasioned by the negligence of an agent of the Federal Housing Commissioner in making an appraisal of the property under the provisions of the state and the regulations issued pursuant thereto. See 12 U.S.C. § 1709(b)(2) and 24 C.F.R. § 200.4(b). The United States does not deny that the appraisal was faulty or that the purchasers were injured thereby but defends on the ground that the plaintiffs' claim arises out of misrepresentation which is excluded from the coverage of the Tort Claims Act by 28 U.S.C. § 2680(h).

The property is located in Alexandria, Virginia. The former owners, in anticipation of selling it, caused an approved lender to make application under 12 U.S.C. § 1709(a) of the Act for a conditional commitment to insure the mortgage and pursuant thereto the property was inspected by an FHA appraiser, who reported that the property was eligible for mortgage at the appraised value of $22,750. The plaintiffs as prospective purchasers were apprised of this fact. Thereupon a contract of sale was executed conditioned upon the purchasers obtaining a loan secured by an FHA mortgage in the sum of $18,800. Therein the sellers agreed to furnish the plaintiffs a written statement of the appraised value as so determined, and this was done upon the settlement date when the purchasers took title to the property.

[fol. 148] The purchasers took possession of the house and several days later substantial cracks appeared in the interior walls and ceilings in all of the rooms, as well as in the cinder blocks in the basement walls. It was then found by FHA officials that cracks were appearing in the exterior walls, and that the one-story sun porch was separating from the east wall, and that the foundations were settling in an unusual manner. These conditions were found to have been caused by the character of the subsoil, which contained a type of clay that quickly disintegrates when exposed to water; and it was ascertained that the underpinning of the foundations would require the expenditure of several thousand dollars.

The pending case was then brought and tried before the District Judge without a jury, who rendered a verdict in favor of the plaintiffs for $8000. The judge called atten-

tion to the amendment to the statute by the act of Congress of August 2, 1954, codified in 28 U.S.C. § 1715(q), whereby the seller of a dwelling approved for mortgage insurance under the state is required to agree to deliver to the purchaser prior to the sale a written statement setting forth the amount of the appraised value of the property as determined by the Commissioner. The Judge held that the statute as amended imposes upon the United States the duty to appraise the property with ordinary care and diligence as a gauge of the fairness of the price to be paid by the purchaser and that neglect of this duty makes the United States liable to the purchaser. He was of the opinion that the appraisal involves not merely a representation on the part of the United States but the performance of a positive act by the government as a direct and immediate service to the purchasers. He found that in this case the plaintiffs, in good faith, relied upon [fol. 149] the appraisal in consummating the purchase and, since serious structural defects in the house subsequently appeared which reasonable care by a qualified appraiser would have discovered, the negligence of the government to perform its statutory duty entitled the plaintiffs to recover the direct loss of $8000 resulting therefrom. Accordingly, a judgment for this amount was rendered against the United States.

The United States on this appeal relies upon the exclusionary section of the Tort Claims Act, which declares in 28 U.S.C. § 2680(h) that the provisions of the statute shall not apply, inter alia, to any claim rising out of misrepresentation or deceit. It has been uniformly held that "misrepresentation" in this context, since it appears in the act in juxtaposition to "deceit", means negligent as well as wilful misrepresentation.[1] We are in accord with this view especially as it is reasonable to suppose that Congress intended to exempt the Government from liability

[1] Jones v. United States, 2 Cir., 207 F.2d 563, cert. den., 347 U.S. 921; National Mfg. Co. v. United States, 8 Cir., 210 F.2d 263, 275-276, cert. den., 347 U.S. 967; Clark v. United States, 9 Cir., 218 F.2d 446, 452; Miller Harness Co. v. United States, 2 Cir., 241 F.2d 781; Anglo-American & Overseas Corp. v. United States, 2 Cir., 242 F.2d 236; Hall v. United States, 10 Cir., 274 F.2d 69.

for misinformation carelessly given by its agents to the public in the wide field of its manifold activities.[2] The Government therefore contends that it has no liability in the pending case, and in support of its position cites a [fol. 150] number of cases in the federal courts, analyzed in footnote,[3] in which, under varying circumstances, it has

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[2] In National Mfg. Co. v. United States, 8 Cir., 210 F.2d 263, 276, the court said that the intent of the section is to except from the Act cases where mere "talk" or mere failure "to talk" on the part of a government employee is asserted as the proximate cause of damage sought to be recovered from the United States.

[3] In Anglo-American & Overseas Corp. v. United States, S.D. N.Y., 144 F. Supp. 635, affirmed 2 Cir., 242 F.2d 236, a merchant purchased certain lots of imported tomato paste, relying upon the fact that it had been admitted into the United States after examination by agents of the United States pursuant to the Pure Food, Drug and Cosmetics Act. Later the merchant endeavored to sell the goods to the United States but they were rejected and condemned because they were found to be adulterated. It was held that the plaintiff could not recover because the duty imposed upon the United States under the statute was owed to the consumers and not to the dealer and, also, because the plaintiff's injury grew out of misrepresentation within the exception of the Tort Claims Act which was applicable, although the misrepresentation flowed from negligence in testing the goods.

In Hall v. United States, 10 Cir., 274 F.2d 69, the plaintiff, who was engaged in the cattle business in New Mexico, complained that he was injured when agents of the United States Department of Agriculture engaged in testing livestock for disease informed him that his cattle were diseased, causing him to sell them for less than their market value, whereas in fact there were no diseased cattle in the herd. It was held that the plaintiff could not recover because the loss was caused, not by the faulty testing of the herd, but by the misrepresentations of the government agents. Whether the duty to inspect was owed to the general public or to the plaintiff was not considered.

In Jones v. United States, 2 Cir., 207 F.2d 563, cert. den. 347 U.S. 921, the plaintiffs sued for loss incurred when they sold their stock in an oil company for less than it was worth after they had asked the United States Geological Survey for information as to the ultimate recovery of oil to be expected from the company's lands and were told, as the result of a negligent estimate by an agent of the United States, that the expected recovery was far less than it turned out to be. It was held that the suit was based on misrepresentation, for which recovery was barred under the statute. Whether the government owed any duty to the plaintiffs

been exonerated from liability for damages caused by negligent misrepresentation of its agents. We can discern no clear line running through these cases which serves as a guide to the solution of the present controversy. In most of them liability could be based only upon misrepresentation by agents of the government since the actions complained of were carried on for the benefit of the public at large and not in the performance of a specific

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was not discussed, but it was pointed out in the opinion of the District Judge, 120 F. Supp. 894, that the members of the geological survey are forbidden by the statute, 43 U.S.C. §31, to execute surveys or examinations for private parties.

In Clark v. United States, 9 Cir., 218 F.2d 446, it was held that the United States was not liable for damages to persons and property caused by flood in the Columbia River, since the evidence showed no negligence on the part of the United States either in its precautions to prevent the flooding of lands or in the issuance of a bulletin to the public to the effect that the flood situation was not dangerous. The court added that even if the flood should have been foreseen and the bulletin was negligently issued, the government was not liable since the misrepresentation therein involved fell within the exception of the Tort Claims Act.

Again, in National Mfg. Co. v. United States, 8 Cir., 210 F.2d 263, cert. den. 347 U.S. 967, the liability of the United States for dissemination by its agents of erroneous flood and weather reports was before the courts. It was held that the government was exonerated from liability for damages from flood waters by the express provision set out in the flood control act and that this provision was broad enough to bar recovery for damages caused by the negligence of government agents in circulating flood and weather reports; and it was also held that negligent conduct in the dissemination of erroneous reports was within the misrepresentation exception of the Tort Claims Act.

In Miller Harness Co. v. United States, 2 Cir., 241 F.2d 781, the plaintiff purchased from the United States certain surplus property described as saddle parts in the invitation to bidders wherein bidders were cautioned to inspect the property, and it was expressly stated that the government made no guarantee as to quantity, kind, character or description. The plaintiff being uncertain as to the character of the saddle parts, telephoned the custodian of the government depot and was told that stirrup irons and stirrup leathers were included in the item. Accordingly, the plaintiff bought the goods; but when they were delivered no stirrup parts or stirrup leathers were included and accordingly he brought suit for their reasonable value. Judgment went against him on the ground that his claim was based merely on misrepresentation.

duty owed to the injured party, *Clark* v. *United States*, 9 Cir., 218 F.2d 446; *Anglo-American & Overseas Corp.* v. *United States*, 2 Cir., 242 F.2d 236; or the statute or contract governing the activity expressly exempted the government from liability for the acts of its agent, *Jones* v. *United States*, 2 Cir., 207 F.2d 563, cert. den. 347 U.S. 921; *National Mfg. Co.* v. *United States*, 8 Cir., 210 F.2d 263. [fol. 151] On the other hand, it has been held that if the government assumes a duty and negligently performs it, a party injured thereby may recover damages from the United States even though the careless performance of the duty may have been accompanied by some misrepresentation of fact. Thus in *Otness* v. *United States*, D.C., Alaska, 178 F. Supp. 647, a shipowner sued to recover for the loss of his vessel due to collision with a submerged channel light which the Coast Guard undertook to locate but negligently failed to find, whereupon it issued an erroneous bulletin that no part of the light remained above the bottom of the sea. It was held that although the bulletin contained a misrepresentation of facts, this did not bring the case within the exemption of the Tort Claims Act or absolve the United States from liability for the negligent performance of a duty which it had voluntarily assumed. In like manner, the United States was held liable under the Federal Tort Claims Act for the negligent operation of a lighthouse in *Indian Towing Co.* v. *United States*, 350 U.S. 61, and for the negligent marking of a wreck in *Somerset Seafood Co.* v. *United States*, 4 Cir., 193 F.2d [fol. 152] 631. In each case liability was based upon the negligent performance of a duty assumed by or resting upon the government. There was no discussion in either case of the statutory exemption of the United States for liability for misrepresentation, but, as pointed out by the District Judge in the court below, misrepresentation was necessarily involved in the negligent marking of the wreck in one case and in the absence of notice of peril to the mariner in the other.

The record in the instant case discloses that the government owed a specific duty to the plaintiffs as purchasers of the property and that they suffered substantial loss from the careless manner in which the duty was performed. The scheme of the National Housing Act, 12

U.S.C. § 1709(a), under which the purchase was made endows the Federal Housing Commissioner with power to [fol. 153] insure a mortgage on a single family residence property if the mortgage complies with certain statutory requirements and involves a principal obligation not in excess of specified fractions of the appraised value of the property, which are placed very high in order to aid a prospective buyer with limited capital to acquire a residence. Application for the insurance must be made by an approved financial institution and frequently is made in advance of the execution of the mortgage. On receipt of the application an appraisal of the property is made to determine whether it meets the standards prescribed by the Commissioner and to fix a valuation for insurance purposes. If the property is approved, a conditional commitment is made to the applicant wherein the Commissioner agrees to insure the property in an amount computed upon its appraised value provided it is found that the purchaser is financially able to carry the mortgage. Obviously the appraisal of the property is an important part of the process. To accomplish this the appraiser inspects the property to ascertain its condition and eligibility and, if if is found eligible, makes an appraisal based on its long-time economic value.

This procedure was designed to effectuate the purpose of the Act, to encourage the construction of housing by giving aid to prospective purchasers, and at the same time to protect the government from a loss that would be incurred by insuring undesirable property. In 1954, the purpose of Congress to protect the purchaser was emphasized and further advanced by the addition to the statute of the amendment set out in 28 U.S.C. § 1715(q) referred to above. This Act directed the Commissioner to require the seller of residential property, covered by an approved mortgage under the statute, to deliver to the purchaser a written statement setting forh the amount of the appraised [fol. 154] value as determined by the Housing Commissioner. The purpose of the new act to inform the purchaser of the value placed upon the property by government appraisal for his own guidance is clear upon the face of the enactment. If there were any doubt about it, it is made clear by the legislative history.

The Senate report upon the National Housing Act of 1954 contains a section entitled "The Protection of the Consumer" in which it was indicated that there was need for a change in the philosophy of the Federal Housing Administration in the administration of the statute, so that the agency, while keeping in mind the objectives of the Act to maintain a high limit of housing production and to protect the insurance fund and the mortgagee from loss, would recognize its responsibility to protect the public interest in general and the rights of homeowners in particular, and at all times to regard it as a primary responsibility to act in the interest of the individual home purchaser and protect him to the extent feasible. See 2 U.C. Code Congressional and Administrative News, p. 2726. The conference report on the measure emphasizes the same purpose. It pointed out that, notwithstanding the fact that there is no technical relationship between the FHA and the individual, it was the intent of Congress that the procedures of the administration should not be used exclusively for the protection of the government and its fund, and attention was drawn to the specific provision of the amended act which requires that the purchaser be given a written statement setting forth the FHA's appraised value of the property so that the purchaser may be informed as to the amount that would be warranted in making the purchase. 2 U.S. Code Congressional and Administrative News, p. 2828.

[fol. 155] Thus, it is abundantly clear that the government owed a specific duty to the plaintiffs in this case even though there was no contractual relationship between them. The situation is similar to that considered by Judge Cardozo in *Glanzer* v. *Sheppard*, 233 N.Y. 236, where it was held that a public weigher, who was employed by the seller of goods and overstated the weight of the merchandise, was liable in damages to the buyer who bought them on the faith of the weigher's certificate. It was pointed out in the opinion that the defendant was not held merely for careless words but for the careless performance of the act of weighing.

So in the pending case, the wrongful conduct complained of does not consist merely or chiefly in the com-

munication to the plaintiffs whereby they were notified that the Housing Commissioner had appraised the property for mortgage purposes at $22,750, but primarily in the negligent appraisal itself whereby they were led to pay more for the property than it was worth. The government takes the narrow ground that the purchasers' loss was not occasioned by the negligent appraisal but by the misrepresentation in the government's report of the appraisal. The communication itself however was not, strictly speaking, a misrepresentation of fact, for it correctly reported that the Commissioner had appraised the property and placed a valuation upon it of $22,750, both of which statements were true. It cannot be denied, however, that there was an element of misrepresentation of fact in the government's conduct when the transaction is considered as a whole. The report sent to the purchasers purported to be and might fairly be accepted by them as an accurate appraisal of the value of the property carefully made so that in effect it amounted to a misstatement [fol. 156] of fact. Hence it might form the basis of an action for misrepresentation under general common-law principles, for it is generally held that one who supplies information for the guidance of others in their business is liable for harm to those who rely upon the information if there has been negligence in obtaining and communicating it, and the person harmed is one for whose guidance the information was supplied. Restatement of Torts, § 552; Prosser on Torts, p. 543.

It does not necessarily follow, however, that the case falls within the exemption of the Tort Claims Act, since it involves not only misrepresentation but also negligent performance of a definite duty owed to the plaintiffs. The real question is whether it was the intent of Congress to absolve the government from liability in every case in which misrepresentation plays merely a part. Misrepresentation, as Prosser shows, runs all through the law of torts and there are many types of wrongful conduct in which there are elements of misrepresentation that are usually grouped under categories of their own. Thus, as the author says (p. 520):

> "* * * A great many of the common and familiar forms of negligent conduct, resulting in invasions of

> tangible interests of person or property, are in their essence nothing more than misrepresentation, from a misleading signal by a driver of an automobile about to make a turn, or an assurance that a danger does not exist, to false statements or non-disclosure of a latent defect by one who is under a duty to give warning. In addition, misrepresentation may play an important part in the invasion of intangible interests, in such torts as defamation, malicious prosecution, or interference with contractual relations. In all such [fol. 157] cases the particular form which the defendant's conduct has taken has become relatively unimportant, and misrepresentation has been merged to such an extent with other kinds of misconduct that neither the courts nor legal writers have found any occasion to regard it as a separate basis of liability."

In view of this situation we do not think that the government is necessarily absolved from liability in every case of wrongful conduct on its part which incidentally embraces misrepresentation. It is abhorrent to common sense to hold that the government can relieve itself from liability for neglect of duty owed to an individual merely by telling him falsely that the duty has been faithfully performed; and it cannot be supposed that Congress had any such idea in mind when it included "misrepresentation" among the exceptions to the statute. Quite clearly the gist of the offense in this case was the careless making of an excessive appraisal so that the home seeker, whom the Commissioner was obligated to protect, was deceived and suffered substantial loss. This was the gravamen of the offense to which the report of the Commissioner was merely incidental. Accordingly, the judgment of the District Court is affirmed.

Affirmed.

[fol. 158] UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

No. 8071.

UNITED STATES OF AMERICA, APPELLANT,

vs.

STANLEY S. NEUSTADT and ROSE-BARBARA Y. NEUSTADT, APPELLEES.

JUDGMENT—April 19, 1960

APPEAL FROM the United States District Court for the Eastern District of Virginia.

THIS CAUSE came on to be heard on the record from the United States District Court for the Eastern District of Virginia, and was argued by counsel.

ON CONSIDERATION WHEREOF, It is now here ordered and adjudged by this Court that the judgment of the said District Court appealed from, in this cause, be, and the same is hereby, affirmed with costs.

MORRIS A. SOPER
United States Circuit Judge.

HERBERT S. BOREMAN
United States Circuit Judge.

A. D. BARKSDALE
United States District Judge.

FILED AUG 19 1960 R.M.F. Williams, Jr. Clerk

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[fol. 159] Clerk's Certificate to foregoing transcript omitted in printing

[fol. 169] SUPREME COURT OF THE UNITED STATES

No. 533, October Term, 1960

UNITED STATES, PETITIONER,

vs.

STANLEY S. NEUSTADT, ET AL.

ORDER ALLOWING CERTIORARI—December 19, 1960

The petition herein for a writ of certiorari to the United States Court of Appeals for the Fourth Circuit is granted, and the case is transferred to the summary calendar.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

☆ U. S. GOVERNMENT PRINTING OFFICE: 1961 583422 685